K.R.RAMAMANI MEMORIAL NATIONAL TAXATION MOOT PROBLEM 2020-21

The Income Tax Department filed a tax case appeal (TCA) before the Hon'ble High Court of Madras u/S.260A of the Income Tax Act, 1961 against the order of the ITAT passed in case of M/s. Vulcan Laboratories Pvt. Ltd. Vs ACIT for the AY 2009-10 raising the following substantial question of law which have been admitted by the Hon'ble High Court and fixed for final hearing:

Whether the Tribunal order is perverse in law in holding that the second proviso of S.40(a)(ia) is curative and thus retrospective in its application?

Annexures: ITAT Order, S.40(a)(ia) and S.201(1) of Income Tax Act, 1961

IN THE INCOME TAX APPELLATE TRIBUNAL CHENNAI 'A' BENCH
BEFORE SHRI F.D.LEGELLO, JUDICIAL MEMBER AND
SHRI ANTHONY VARDON, ACCOUNTANT MEMBER
ITA No. 1991/Mds/2017, Assessment Year: 2009-10

Vulcan Laboratories Pvt. Ltd. Vs. Dy.CIT, Circle 12(2)
New No 75A, Dr.RKSalai, Chennai .
PAN: AADCM3491M
(Appellant/Assessee) (Respondent)

For Revenue: Shri Aziz Alam
For Assessee: Shri Raman Gopalakrishnan
Date of Hearing & Pronouncement : 15/10/20

O R D E R (Per Bench)

Main Ground raised by the assessee is as follows:
"2. Disallowance of payment of Rs.41,32,675/- payment to Markiv India Pvt. Ltd. for technical consultancy services u/S. 40(a)(ia) of the Act for failure to withhold any taxes on aforesaid payment"

3. Brief facts of the case are that the assessee company, engaged in software business, filed its return of income for the A.Y. 2009-10 on 30.9.2009 admitting a total profit of Rs.89,17,34,256/- under normal provisions of the Income Tax Act, 1961 (the Act). The return was initially processed u/s 143(1) of the Act and the case was selected for scrutiny under CASS. Notices u/s 143(2) of the Act and u/s 142(1) were issued and responded to by the assessee.

3.1 The Assessing Officer (AO) observed a payment by the assessee to one Markiv India Pvt. Ltd was made for Rs.41,32,675/- and asked for details of the same. The assessee in its written letter dated 21.9.2011 had submitted that payments to Markiv India Pvt. Ltd. were for technical services but on further enquiry it was established that the assessee did not withhold any tax on these payments i.e., no TDS was deducted. The AO passed an Order dated 21.12.2011 disallowing the entire payment of Rs.41,32,675/- u/S.40(a)(ia) of the Income Tax Act, 1961 in the hands of assessee/payer (Vulcan Labs).

3.2 Before AO and CIT(A) (who merely upheld the AO) and ITAT, the Ld. Counsel of Assessee took the same arguments which we condense herein below.

3.3 The Learned Counsel for assessee pointed out that the recipient Markiv India Pvt. Ltd. has offered this payment from Vulcan Labs for tax i.e., this income from Vulcan Laboratories has been taken into account by Markiv India while computing its taxable income. And according to the Learned Counsel If the recipient has offered the income to tax then the disallowance u/S 40(a)(ia) is fundamentally erroneous.

3.4 Towards this, Learned Counsel explained that that if a payer fails to withhold tax the Department could proceed against the assessee/payer u/S.201(1) i.e., holding the payer as an "assessee in default" (or) can proceed against the assessee/payer u/S.40(a)(ia) wherein the payment deduction i.e., expenditure claim, is entirely disallowed in hands of assessee/payer.

3.5 He further pointed out that first Proviso of S.201(1) sets down three conditions to show that IF the recipient (in this case Markiv India Pvt.Ltd.) has offered the amounts paid for tax and provides a certificate from a Chartered Accountant in Form 26A certifying the same then the payer (assessee/Vulcan Labs) cannot held to be an "assessee in default" and can't be proceeded against for not withholding taxes as essentially the amount in question has suffered tax – maybe not as a deduction by the payer but as income by the payee. So, earlier this Proviso applied only to proceedings u/S.201(1) but the second proviso to S.40(a)(ia) brought its applicability to S.40(a)(ia) too. In short, if the recipient offered the payment to tax and prescribed CA certificate provided, disallowance u/S.40(a)(ia) disallowance too could not be sustained.

3.6 The Learned Counsel for Assessee points out that on all the above there is really no dispute between department and assessee but where there is a cleavage of opinion is that the second Proviso of S.40(a)ia) referred to and relied on above was inserted only w.e.f. 1-4-2013 but the impugned AY is 2009-10 and so the Department is of the view that the second Proviso doesn't apply to the impugned AY as it is specifically inserted prospectively and hence *even if* the recipient has offered to tax the payments by Vulcan Labs in AY 2009-10 it doesn't save the payer (Vulcan Labs) from s.40(a)(ia) disallowance.

3.7 To this, the Learned Counsel's plea is that the second Proviso was only curative and hence should be applied retrospective and this is the crux of this entire appeal.

3.8 The Learned Counsel substantiates his retrospectivity stance by submitting it was always the case in S.201(1) that the recipient having paid the tax the payer could not be penalized for not withholding as held in *CIT vs. Hindustan Coca Cola Beverages Pvt.Ltd. [293 ITR 226]* and if this were not the case, such as assumed by Department in S.40(a)(ia) prior to the insertion of the second proviso, the Department could essentially end up *doubly taxing* the same amount in certain cases like the instant assessee's case (for example: disallowed in payers hands and so payer paying tax on it and it may also have been offered in recipients hands, so recipient also paying tax on it). So, this proviso according to the Learned Counsel only *cures* this defect in S.40(a)(ia) and therefore must be held to be retrospective and applicable to AY 09-10.

3.9 The Learned Counsel for assessee relied heavily on ***CIT vs. Ansal Landmark Township in ITA 160/2015 dated 26.8.2015*** wherein S.40(a)(ia's second proviso was held to be curative and hence retrospective. The Learned

Counsel additionally pointed out that it should be interpreted in the same vein as the SC judgment in *CIT vs. Calcutta Export Company in CA Nos. 4339-4340 of 2018 dated 24.4.2018* which held the change made in Finance Act 2010 to S.40(a)(ia), to allow payments of deducted TDS amount up to due date of return, as retrospective .

3.10 On the other hand the Learned DR pointed out that this was a substantive provision relating to payment and strongly relied on ***Thomas George Muthoot Vs CIT (Kerala HC) in ITA 278/2014 dated 28.8.2014*** wherein it was held second proviso to S.40(a)(ia) is prospective in nature. The Learned DR pointed out that the SC in *Shree Choudhary Transport Company Vs ITO (Supreme Court) in CA No. 7865 of 2009 dated 29.7.2020* held that the amendment in first proviso by Finance Act 2014 w.e.f 1-4-2015 to restrict the disallowance to 30% of the payment is substantive and hence prospective and the same ratio must be adopted in this case.

3.11 We are of the view that on facts it is not disputed by the Department that the recipient (Markiv India P. Ltd) offered the payments from the assessee to tax. Also, w.e.f 1-4-2013 it is not disputed that the disallowance u/s 40(a)(ia) wouldn't stand. The only issue is the retrospective application of the second Proviso to S.40(a)(ia). We believe the Delhi High Court in *Ansal Landmark Township* takes the right view that second proviso is retrospective in its application as it is curative in nature. Doubly taxing an amount would be against the basic canons of taxation and the Delhi High Court judgment has only followed the jurisprudence of a series of similar judgments on retrospectivity such as ***Allied Motor v. CIT [224 ITR 677], CIT vs. Alom Extrusions Ltd. [319 ITR 306]***. Appeal allowed in favour of the assessee.

Sd/-
Accountant Member

Sd/-
Judicial Member

Extract of current S.40(a)(ia) of Income Tax Act, 1961
[second Proviso which is in dispute is highlighted]

S.40(a)(ia) : Amounts not deductible

(ia) thirty per cent of any sum payable to a resident, on which tax is deductible at source under Chapter XVII-B and such tax has not been deducted or, after deduction, has not been paid on or before the due date specified in sub-section (1) of section 139 :

Provided that where in respect of any such sum, tax has been deducted in any subsequent year, or has been deducted during the previous year but paid after the due date specified in sub-section (1) of section 139, thirty per cent of such sum shall be allowed as a deduction in computing the income of the previous year in which such tax has been paid :

Provided further that where an assessee fails to deduct the whole or any part of the tax in accordance with the provisions of Chapter XVII-B on any such sum but is not deemed to be an assessee in default under the first proviso to sub-section (1) of section 201, then, for the purpose of this sub-clause, it shall be deemed that the assessee has deducted and paid the tax on such sum on the date of furnishing of return of income by the payee referred to in the said proviso.

Extract of current S.201(1) of Income Tax Act, 1961

Consequences of failure to deduct or pay.

S.201. (1) *Where any person, including the principal officer of a company,—*

(a) who is required to deduct any sum in accordance with the provisions of this Act; or

(b) referred to in sub-section (1A) of section 192, being an employer,

does not deduct, or does not pay, or after so deducting fails to pay, the whole or any part of the tax, as required by or under this Act, then, such person, shall, without prejudice to any other consequences which he may incur, be deemed to be an assessee in default in respect of such tax:

Provided that any person, including the principal officer of a company, who fails to deduct the whole or any part of the tax in accordance with the provisions of this Chapter on the sum paid to a payee or on the sum credited to the account of a payee shall not be deemed to be an assessee in default in respect of such tax if such payee—

(i) has furnished his return of income under section 139;

(ii) has taken into account such sum for computing income in such return of income; and

(iii) has paid the tax due on the income declared by him in such return of income,

and the person furnishes a certificate to this effect from an accountant in such form as may be prescribed:

Note: See Rule 31ACB of IT Rules and Form No.26A